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JAMES R. BROWNING,

IN THE

Supreme Court of the United States

October Term, 1958

No. 409

ESTATE OF JOHN IVERSON, ET AL.,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

MARDRID REITE DAVISON,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

ESTATE OF JOHN IVERSON, ET AL., AND ELLEN MYERS AND CHARLOTTE SCHAEFFER, CO-EXECUTRICES OF THE ESTATE OF ALVILDA IVERSON, DECEASED,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

ELLEN MYERS AND CHARLOTTE SCHAEFFER, CO-EXECUTRICES OF THE ESTATE OF ALVILDA IVERSON, DECEASED,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

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COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

The above-named petitioners pray that a writ of certiorari issue to review the judgment of the United States Court of

Appeals for the Eighth Circuit, entered in the above-entitled cases on the 9th day of May, 1958.

CITATION TO OPINION BELOW

The opinion of the Court of Appeals for the Eighth Circuit is reported at 255 F. 2d 1. A copy of said opinion is appended hereto in the Appendix. The opinion of the Tax Court of the United States is officially reported in 27 T.C. 786. Since the opinion of the Tax Court appears at page 132 of the Record printed for the use of the Circuit Court, nine copies of which are filed herewith, that opinion is not appended to this petition but rather is omitted in accordance with Rule 23 (1) (i) of the Rules of this Court.

JURISDICTION

The judgment of the Court of Appeals was dated and entered the 9th day of May, 1958. The jurisdiction of this Court is invoked under *28 U.S.C. Section 1254 (1).*

QUESTION PRESENTED

Whether the term "gross income" as used in Section *275 (c)* of the *Internal Revenue Code of 1939* means gross receipts before diminution by cost of goods sold so that *Section 275 (c)* is applicable only where the taxpayer's omitted receipts exceed 25% of his reported gross receipts before reduction for costs of goods sold.

STATUTE INVOLVED

The statute involved in this matter is *Section 275 (c)* of the *Internal Revenue Code of 1939.*

STATEMENT OF THE CASE

The sole issue in this case is whether assessments by the Commissioner of asserted tax deficiencies were barred by the three-year statute of limitations provided in the *Internal Revenue Code of 1939*. Under the *1939 Code* the general statute of limitations governing the assessment of federal income tax deficiencies is fixed at three years from the date on which the taxpayer filed his return (see § *275 (a)* thereof), *53 Stat. 86*, except in cases involving intentionally false or fraudulent returns, where a tax may be assessed at any time (see § *275 (a)*, *53 Stat. 87*). A special five-year period of limitations is provided when a taxpayer, even though acting in good faith, "omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return * * *." § *275 (c)*, *53 Stat. 86*.

The Commissioner asserted deficiencies in each of the above-named taxpayers' income taxes for each of the calendar years 1947 and 1948 more than three but less than five years after the returns were filed. There was a claim that taxpayers had inaccurately reported their gross receipts. This arose by reason of the fact that the taxpayers reported sales on a cash basis of accounting. The Commissioner changed the taxpayers to an accrual basis of reporting sales.

The instant cases were consolidated for purposes of trial in the Tax Court and in the Court of Appeals and are consolidated here in accordance with the practice of this Court. The respective petitioners, the taxable years involved and the income tax deficiencies proposed by the Commissioner of Internal Revenue are as follows (R. 133):

Circuit Court Docket No.	Tax Court Docket No.	Petitioner	Taxable Year	Deficiency
15928	48050	Estate of John Iverson, et al.	1947	$48,821.5
15929	48052	Mardrid Reite Davison	1947	14,637.8
15930	48053	Estate of John Iverson, et al., and Ellen Myers and Charlotte Schaeffer, Co-executrices of the Estate of Alvilda Iverson, Deceased	1948	23,747.8
15931	48054	Ellen Myers and Charlotte Schaeffer, Co-executrices of the Estate of Alvilda Iverson, Deceased	1947	22,220.9

During the years in issue, John Iverson and Alvilda Iverson, both now deceased, were husband and wife. For 1947 each timely filed a separate individual income tax return, and for 1948 they timely filed a joint income tax return (R. 109). Mardrid Reite Davison timely filed a separate individual income tax return for each of the years 1947 and 1948 (R. 109).

During each of the years 1947 and 1948, John Iverson, Alvilda Iverson and Mardrid Reite Davison owned interests in the following partnerships which were engaged in the wholesale and retail selling of electrical supplies and appliances (R. 110):

Partner	Mandan Electric Company Mandan, N.D.	Maytag Electric Company Glasgow, Mont.	Maytag Electric Company Minot, N.D.
John Iverson	50%	50%	33 1/3%
Alvilda Iverson	50%		33 1/3%
Mardrid Davison		50%	33 1/3%
Totals	100%	100%	100%

In addition, during the same years, John Iverson owned, and operated with one O. G. Aal, a store engaged in the same type of business at Williston, North Dakota (R. 110).

The books of these four partnership businesses were currently kept on the accrual basis of accounting (R. 73, 111), but at the end of each year adjustments were made to exclude the uncollected credit sales from income (R. 73, 87). As a consequence, the returns of the partnerships and of petitioners reported their sales as income in the year in which collected (R. 73, 74, 87).

This system of accounting had been consistently applied and followed by petitioners in reporting their income for at least twelve years prior to the taxable years here involved (R. 73, 74). The returns of petitioners and their business books and records were examined by the Internal Revenue Service in 1942 and no change in this system of accounting was required or proposed (R. 74, 89).

At the time of the 1942 examination, petitioner's system of account resulted in their paying more tax than would have been due under the strict accrual method of reporting income, which the government seeks to use for 1947 and 1948, since in 1940, 1941 and 1942 all the outstanding accounts receivable of these businesses, including receivables arising from sales made as far back as 1929, were collected and reported as taxable income (R. 74). This was discussed very thoroughly with the revenue agent who checked the books in 1942 and he advised petitioners that although they were being overtaxed at that time, the situation would equalize itself when petitioners' receivables increased (R. 74).

In 1947 and 1948, a seller's market existed in the electric and appliance business and substantial sales on credits were made by each of the four businesses in which the petitioners

were partners (R. 75). The incomes of these businesses were computed and reported for these years, as in the prior taxable periods, in accordance with petitioners' regular system of accounting which reflected income as and when collected (R. 73, 74, 87). However, when the Internal Revenue Service examined petitioners' returns for 1947 and 1948, it proceeded just to the contrary of the action it took in 1942, and insisted that petitioners' business income be reported on the strict accrual basis so as to include the uncollected credit sales of these businesses as of the end of 1947 and 1948 (R. 68, 69).

Not one of the petitioners omitted for either of the years 1947 or 1948 an amount equal to 25% of his share of the gross receipts reported on the partnership returns. Thus, for 1947 John Iverson's reported gross receipts from business and nonbusiness sources was $573,560.56 (R. 135, 137) and his share of the uncollected credit sales for that year was $43,994.88 (R. 137). This made his accrual basis gross receipts $617,555.44 which is but 7.67% more than reported on the cash basis. Alvilda Iverson's reported gross receipts on the cash basis in 1947 were $309,797.62 (R. 135, 138) and her share of the uncollected credit sales for that year was $19,387.02 (R. 137). Her accrual basis receipts were therefore $329,184.64 which is 6.26% more than reported on cash. For 1948, John and Alvilda Iverson jointly reported gross receipts of $1,351,898.71 (R. 135, 138) and their share of the uncollected credit sales for the year was $52,520.80 (R. 137). Their accrual basis gross receipts therefore exceeded reported gross receipts by only 3.88%. Mardrid Davison reported gross receipts of $234,066.13 and $367,189.73, respectively, for 1947 and 1948 (R. 135, 138). Her share of uncollected credit sales was $17,848.18 for 1947 and

$13,039.72 for 1948 (R. 137). Her accrual basis gross receipts therefore exceeded her reported gross receipts by only 7.63% in 1947 and 3.55% for 1948.

The statutory notices of deficiency covering the years 1947 and 1948 were issued to petitioners on January 30, 1953 (R. 7, 22, 41, 60). This date was more than three but less than five years after the petitioners had filed their tax returns for the years 1947 and 1948.

The statutory notices were untimely unless the extended limitations' period under *Section 275 (c)* of the *Internal Revenue Code of 1939, 26 U.S.C.A. § 275 (c)* applies. The Tax Court determined, and the Court of Appeals affirmed that each petitioner had omitted from gross income amounts properly includible therein which were in excess of 25 per cent of the amount of his reported gross income and that therefore the conditions of *Section 275 (c)* were satisfied.

REASONS FOR GRANTING THE WRIT

This case was decided by the United States Court of Appeals for the Eighth Circuit on May 9, 1958, which was prior to the date this Court handed down its opinion in *The Colony, Inc. v. Commissioner of Internal Revenue* (U. S. Supreme Court, June 9, 1958) —— U. S. ——. By reason of that fact, the Court of Appeals did not have the benefit of the opinion of this Court at the time it rendered its decision. The interpretation given *Section 275 (c)* of the *Internal Revenue Code of 1939* by the Court of Appeals for the Eighth Circuit in this case is contrary to that of this Court expressed on June 9, 1958.

After the opinion of this Court in *The Colony, Inc.* case was handed down, petitioners herein filed a motion for recall of mandates and a petition for rehearing, with the

Court of Appeals for the Eighth Circuit. That motion and petition was filed June 29, 1958. The Court of Appeals for the Eighth Circuit, in a per curiam opinion filed July 25, 1958, a copy of which is reproduced in the appendix hereto, denied the motion for recall of mandates and leave to file the petition for rehearing. In that opinion the Court of Appeals for the Eighth Circuit assumed it had jurisdiction to recall the mandates, but stated that petitioners had not made sufficient showing to entitle them to file a petition for rehearing out of time. Rule 15 (a) of that court requires that petition for rehearing be filed "not later than twenty days after the filing of an opinion."[1]

The Court of Appeals' opinion was filed on May 9, 1958, and the opinion of this Court on June 9, 1958. Thus, the twenty-day period within which to file a petition for rehearing with the Court of Appeals had already expired prior to the time that this Court rendered its decision in *The Colony, Inc.* case. Nevertheless, the Court of Appeals in its per curiam decision determined that circumstance was not sufficient cause for waiver of the rule. Thus, this petition for writ of certiorari.[2]

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[1]The petition for rehearing was not made a part of the record certified by the Clerk for the Court of Appeals. The Clerk's explanation for the failure to so include it is that the Court refused leave to file the petition and therefore, technically it cannot be a part of this record. However, it is included in the Appendix. Clearly it was filed with the Circuit Court, as that Court's opinion denying the right to file it so obviously demonstrates.

[2]The Court of Appeals for the Ninth Circuit on June 25, 1958, by a per curiam opinion, reversed the Tax Court in a similar situation following this Court's decision in *The Colony, Inc.*, case. See *Arthur L. Lawrence, et al. v. Commissioner of Internal Revenue*, 9 Cir. (1958), —— F. ——.

This Court has, pursuant to timely application by an order signed by Mr. Justice Harold H. Burton dated July 17, 1958, extended to October 6, 1958, the time within which to file this petition for a writ of certiorari.

The pertinent provisions of the *1939 Code* applicable to this case are:

"Sec. 275. Period of Limitation Upon Assessment and Collection.

"Except as provided in section 276—

"(a) General Rule.—The amount of income taxes imposed by this chapter shall be assessed within three years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period.

* * *

"(c) Omission from Gross Income.—If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 5 years after the return was filed.

"Sec. 276. Same—Exceptions.

"(a) False Return and No Returns.—In the case of a false or fraudulent return with intent to evade tax or a failure to file a return the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time.

"(b) Waiver.—Where before the expiration of the time prescribed in section 275 for the assessment of the tax, both the Commissioner and the taxpayer have consented in writing to its assessment after such time, the tax may be assessed at any time prior to the expiration of the period agreed upon. The period so agreed upon may be extended by subsequent agreements made before the expiration of the period previously agreed upon."

There is no claim in these cases that false or fraudulent returns were filed or that waivers have been given. The Commissioner relied entirely on *Section 275 (c)* in asserting the deficiencies here involved.

In *The Colony, Inc.* case it was necessary for this Court to construe the meaning of the critical language of *Section 275 (c)* of the *Internal Revenue Code of 1939* involved herein, which is, "omits from gross income an amount properly includible therein." In reversing the court below in that case, this Court flatly held that *Section 275 (c)* applies only to omissions of gross receipts and not to omissions of gross income as claimed by the government. This Court further held that its construction of *Section 275 (c)* of the *1939 Code* "is in harmony with the unambiguous language of § *6501 (e) (1) (A)* of the *Internal Revenue Code of 1954*," which specifies that the requisite minimum omission of 25% is to be determined by comparing the omitted gross receipts with the reported gross receipts.

In its opinion originally handed down in these cases, the Court of Appeals for the Eighth Circuit made the following observations:

> " 'Gross income' is not defined in the Internal Revenue Code of 1939. The parties agree that 'gross income,' as the term is used in section 275 (c), does not mean gross receipts, but, instead, means gross receipts reduced by cost of goods sold."

The foregoing statement is not accurate. The petitioners at no time, in their brief or elsewhere, ever agreed that "gross income" as used in the *1939 Code* meant "gross receipts reduced by the cost of goods sold." Quite to the contrary, in petitioners' brief to the Court of Appeals the following statement was made:

"In reaching its conclusion that the petitioners were subject to assessment for the 1947 and 1948 deficiencies asserted against them in the government's statutory notices of deficiency, the Tax Court stated in its opinion below (R. 142-143):

> 'A comparison of the unreported credit sales figures with the individual returns discloses that each petitioner's proportionate share of the omitted amounts is far in excess of 25 per cent of the gross income stated in each corresponding individual return. * * * Consequently, we hold that for the years 1947 and 1948 respondent has established that petitioners omitted from gross income amounts properly includible therein which are in excess of 25 per cent of the amounts of gross income stated in the returns. It therefore follows that the notices of deficiency, which were mailed within five years after the returns were filed, were timely.'

"In so holding, the Tax Court was in error even if it be assumed *arguendo*, that the Commissioner of Internal Revenue can unilaterally change the method of accounting which petitioners had consistently employed over the years in reporting their income. The error of the Tax Court in this regard becomes readily apparent when it is noted that the Tax Court compared 'omitted gross receipts' with 'reported gross income' in determining whether or not Section 275 (c) of the 1939 Code applied. Such a comparison of unlikes, i.e., gross receipts with gross income, is, of course, wholly unwarranted. Section 275 (c) of the 1939 Code provides for the comparison of the taxpayer's actual gross income with his reported gross income and specifies that the five-year limitations period applies only where actual gross income exceeds reported gross income by more than 25 per cent. As indicated below, if the Tax Court had made its comparison

on the proper basis, it would have found that the requisite minimum omission did not exist.

"In applying the provisions of Section 275 (c) of the 1939 Code, it is necessary first to clearly fix what is meant by the term 'gross income' since the specified omission of in excess of 25 per cent relates to 'gross income.' This term is not defined in the 1939 Code, therefore it is necessary to look elsewhere for its definition. In its prior decisions, e.g., Jack Rose v. Commissioner, 24 T.C. 755, (1955), the Tax Court has ruled that the 'gross income' to which Section 275 (c) refers is not gross receipts but is instead gross receipts reduced by the cost of goods sold. On the other hand, Section 6501 (e) (1) (i) of the Internal Revenue Code of 1954 defines 'gross income' for purposes of the extended limitations period under the 1954 Code as being equivalent to gross receipts without reduction for the cost of goods sold.

"Regardless of which of these two concepts of gross income is adopted for purposes of applying Section 275 (c), it is clear that the same concept must be applied in determining both parts of the comparison so that the omission from gross income and the reported gross income are computed with a like procedure. This the Tax Court did not do, for, as the above-quoted portion of its opinion reflects, it compared omitted gross receipts with reported gross income, the latter being reported gross receipts less reported cost of goods sold.

"Had the Tax Court compared omitted gross receipts with reported gross receipts, the comparative percentage of omission as to each petitioner would have been less than 8% which is, of course, well below the requisite minimum omission of 25 per cent."

It is undisputed that not one of these petitioners omitted from reported gross receipts an amount in excess of 25% thereof.

Under the decision of this Court in *The Colony, Inc.*, supra, where the omission from gross receipts is not in excess of 25% of the reported gross receipts, the statute of limitations is not held open for the 5-year period under *Section 275 (c)*. The Court of Appeals, however, held in the instant cases that in view of the fact that the omission of gross receipts was more than 25% of the reported gross profit, which is gross receipts reduced by cost of goods sold, the statute of limitations was held open under *Section 275 (c)*.

This Court, in its opinion in *The Colony, Inc.*, supra, decided this specific point and observed:

> "We granted certiorari because this decision conflicted with rulings in other Courts of Appeals on the same issue, and because the question as to the proper scope of § 275 (c), although resolved for the future by § 6501 (e) (1) (A) of the Internal Revenue Code of 1954, p. ...., infra, remains one of substantial importance in the administration of the income tax laws for earlier taxable years.
>
> * * *
>
> "Finally, our construction of § 275 (c) accords with the interpretations in the more recent decisions of four different Courts of Appeals. See note 2, supra. The force of the reasoning in these opinions was recognized by the Court of Appeals in the present case, which indicated that it might have agreed with those courts had the matter been res nova in its circuit. 244 F. 2d at 76. And without doing more than noting the speculative debate between the parties as to whether Congress manifested an intention to clarify or to change the 1939 Code, we observe that the conclusion we reach is in harmony with the unambiguous language of § 6501 (e) (1) (A) of the Internal Revenue Code of 1954."

Section 6501 (e) (1) (A) of the *Internal Revenue Code of 1954* referred to by the Supreme Court of the United States provides as follows:

"§ 6501. Limitations on assessment and collection.

"(e) Omission from gross income.—Except as otherwise provided in subsection (c)—

"(1) Income taxes.—In the case of any tax imposed by subtitle A—

"(A) General rule.—If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—

"(i) In the case of a trade or business, the term 'gross income' means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and

"(ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary or his delegate of the nature and amount of such item."

The first paragraph of *Section 6501 (e) (1) (A)* is identically the same in wording as *Section 275 (c)* of the *Internal Revenue Code of 1939* except that the time limit is 6 years instead of 5. However, the second paragraph of *Section 6501 (e) (1) (A)* specifically defines the term "gross income" to be "gross receipts," that is, the total amounts received or accrued

from the sale of goods or services *prior* to diminution by the cost of such sales or services.

It is this definition of "gross income" that this Court has specifically adopted in construing *Section 275 (c)* of the *1939 Code*, with the result that "gross income" is to be treated as synonymous with "gross receipts" for purposes of applying *Section 275 (c)*. This, of course, is exactly contrary to the hypothesis upon which the Court of Appeals bottomed its decision in these cases.

In view of the undisputed fact that none of the petitioners herein omitted an amount of gross receipts, even on the accrual basis of accounting, that is in excess of 25% of his reported gross receipts, or, in other words, "gross income" as computed prior to diminution by the cost of sales, it is submitted that the writ of certiorari should be granted for the reason that there is a direct conflict between the decision of this Court in *The Colony, Inc.* case and the decision of the Court of Appeals for the Eighth Circuit in the instant proceeding. In view of this Court's decision in *The Colony, Inc.*, a summary reversal of the judgment of the Circuit Court in these cases appears appropriate. *Helvering v. Wiese*, 292 U. S. 614, 54 S. Ct. 862.

Respectfully submitted,

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APPENDIX

UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

No. 15,928

Estate of John Iverson, et al., Petitioners,
v.
Commissioner of Internal Revenue, Respondent.

Petition to Review Decision of The Tax Court of the United States.

No. 15,929

Mardrid Reite Davison, Petitioner,
v.
Commissioner of Internal Revenue, Respondent.

Petition to Review Decision of The Tax Court of the United States.

No. 15,930

Estate of John Iverson, et al., and Ellen Myers and Charlotte Schaeffer, co-executrices of the Estate of Alvilda Iverson, Deceased, Petitioners,
v.
Commissioner of Internal Revenue, Respondent.

Petition to Review Decision of The Tax Court of the United States.

No. 15,931

Ellen Myers and Charlotte Schaeffer, co-executrices of the Estate of Alvilda Iverson, Deceased, Petitioners,
v.
Commissioner of Internal Revenue, Respondent.

Petition to Review Decision of The Tax Court of the United States.

[May 9, 1958]

Joseph A. Maun (William R. Busch, Burton G. Weisberg, and Bundlie, Kelly and Maun were with him on the brief) for Petitioners.

Joseph Kovner, Attorney, Department of Justice (Charles K. Rice, Assistant Attorney General; and Lee A. Jackson, A. F. Prescott, and Kenneth E. Levin, Attorneys, were on the brief) for Respondent.

Before GARDNER, Chief Judge, and VOGEL and VAN OOSTERHOUT, Circuit Judges.

VAN OOSTERHOUT, Circuit Judge.

These are petitions to review decisions of the Tax Court (opinion reported 27 T.C. 786) upholding the Commissioner's determination of income tax deficiencies for the years 1947 and 1948 against the Estate of John Iverson,[1] Alvilda Iverson,[2] and Mardrid Davison. The petitions for review were timely. This court has jurisdiction.

The four petitions before us involve common questions of law and fact. The cases were consolidated in the Tax Court and are consolidated here. The tax liability in these cases arises out of the Commissioner's determination that John and Alvilda Iverson and Mardrid Davison, hereinafter called the taxpayers, were required to include as income in their tax by four stores engaged in the retail and wholesale selling of electrical appliances, fixtures, and supplies. John and returns in the year of sale their share of the credit sales made Alvilda Iverson were husband and wife. Mardrid Davison is

[1]John Iverson died while the proceedings were pending in the Tax Court. The executrices of his estate were substituted as petitioners in his place.

[2]Alvilda Iverson died while the proceedings were pending in this court. The executrices of her estate were substituted as petitioners in her place.

a daughter of Alvilda Iverson by a former husband. The taxpayers owned three of the stores in partnership in varying proportions. The fourth store was owned by John Iverson individually.

The books of all the stores were kept upon an accrual basis. At the end of each taxable year adjustments were made eliminating all credit sales. Taxpayers reported only cash sales for income tax purposes. The credit sales were reported for tax purposes in the year collection was made. The stores all used inventories. Costs of goods sold were determined by adding to the beginning inventory the cost of merchandise purchased for sale, plus freight and excise taxes, less purchase discounts and credits, and subtracting the inventory on hand at the end of the year.

Upon audit of the 1947 and 1948 returns, the Commissioner insisted that credit sales made during each year be accounted for as income. All tax liability here involved results from the inclusion of the credit sales as income for the year of sale. Deficiency notices were mailed on January 30, 1953. This date was more than three years but less than five years after the filing of petitioners' returns for 1947 and 1948. Under the three year statute of limitations, the assessments were barred at the time they were made. Section 275(a) of the Internal Revenue Code of 1939. The Commissioner contends each taxpayer here omitted from gross income an amount includible therein in excess of 25 per cent of gross income stated in the returns, and then hence the five year statute of limitations provided for by section 275(c) is applicable and the assessments were timely.

Taxpayers contend that the five year statute of limitations does not apply for the following reasons:

1. The Commissioner and the Tax Court erred in determining that the uncollected credit sales of the taxpayers'

business enterprises should be included as reportable gross receipts for the year in which such sales were made; and

2. Even if the unreported credit sales are treated as income, the Commissioner has failed to prove that there was an omission from gross income on the part of any taxpayer equal to 25 per cent of his reported gross income.

We shall first determine whether the Tax Court correctly decided that the taxpayers were required to account for their credit sales in the year such sales were made.

Section 41 of the Internal Revenue Code of 1939 provides in part that, if the method of accounting regularly employed by the taxpayer "does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income." Section 29.22(c)-1 of Regulations 111, promulgated under the Internal Revenue Code of 1939, provides:

> "*Need of inventories.*—In order to reflect the net income correctly, inventories at the beginning and end of each taxable year are necessary in every case in which the production, purchase, or sale of merchandise is an income-producing factor. * * *"

The record shows without dispute that the purchase and sale of merchandise is an income-producing factor in taxpayers' business enterprises. Hence, inventories are required by the regulation. The taxpayers have consistently used inventories in computing their income from their stores, and they do not here contend that they were not required to use inventories. Taxpayers do contend that the Commissioner has failed to establish that the method of accounting used by the taxpayers does not clearly reflect their income.

Section 29.41-2 of Regulations 111 provides in part that "in any case in which it is necessary to use an inventory, no

method of accounting in regard to purchases and sales will correctly reflect income except an accrual method." The portion of the regulations just quoted appeared in substantially the same language in section 23 of Regulations 65 promulgated in 1924, and has appeared in all intervening regulations. Treasury regulations and interpretations which are consistent with statute and have remained in effect for a long period of time and have not been altered by congressional action should be given considerable weight. *Corn Products Refining Co.* v. *Commissioner*, 350 U.S. 46, 53; *Helvering* v. *Winmill*, 305 U.S. 79, 83; Mertens Law of Federal Income Taxation, Vol. 1, § 320.

The taxpayers make no attack upon the constitutionality or validity of the regulations. They do place considerable reliance upon *Goodrich* v. *Commissioner*, 8 Cir., 243 F.2d 686. In that case the taxpayer, without obtaining permission from the Commissioner, changed from a hybrid system of accounting to a strict accrual system. The court held that under the applicable law the taxpayer could not be charged with having impliedly agreed to accept whatever terms or conditions the Commissioner might see fit to impose by way of appropriate adjustment, and that the Commissioner "cannot, of his own accord, and over the objection of the taxpayer, impose adjustments which change the tax status of income, as previously existing, to a different year." The court also held that the question of whether the taxpayer, under the circumstances, had a right to change his method of accounting without the Commissioner's consent had not been raised in the Tax Court. The court does make the following statement upon which the taxpayers rely (pp. 690-691):

> "Moreover, we are not prepared to declare abstractly and absolutely that the requirement of the regulation for

the use of an accrual method, where business inventories are involved, leaves no room for the taxpayer lawfully to have employed the hybrid method of accounting and return, which he here did, or no power in the Commissioner to have allowed him, or to be able to require him to continue, to do so, on the facts and elements of his particular situation."

This court in the *Goodrich* case was not squarely confronted with the problem which we now face, and made no decision on the issue of the Commissioner's right to insist that taxpayers required to use an inventory must report income on an accrual basis. The court stated, "These questions we shall leave to a more specific and a more illuminating setting than the present record provides."

In our present case we are compelled to decide whether, by virtue of section 41, heretofore quoted, the Commissioner is authorized to insist that taxpayers account for credit sales in the year of sale. Section 29.41-2, in clear and unambiguous language, provides that where taxpayers are required to use inventories only the accrual method of accounting will correctly reflect income in regard to purchases and sales. The regulation is in no way inconsistent with the provisions of section 41. The validity of the regulation has been consistently upheld. *Herberger* v. *Commissioner*, 9 Cir., 195 F.2d 293, 295; *Caldwell* v. *Commissioner*, 2 Cir., 202 F.2d 112, 114; *Welp* v. *United States*, N.D. Iowa, 103 F.Supp. 551, 553, reversed on other grounds 8 Cir., 201 F.2d 128; *Boynton* v. *Pedrick*, S.D. N.Y., 136 F.Supp. 888, affirmed 2 Cir., 228 F.2d 745; Mertens Law of Federal Income Taxation, Vol. 2, § 16.03.

In the *Caldwell* case, supra, the court states (p. 114):

"• • • The use of inventories in computing income results in stating the expenses of a year's operations in terms of the cost of the goods actually sold during

that year. Thus the profit from these operations will be stated accurately only if the income from all sales made during the year is taken into consideration. This requires use of the accrual method of determining income, since the cash receipts methods obviously does not reflect the actual sales made during the year where, as in the present case, a substantial part of these sales—from 90 to 95 per cent according to the finding—is made on credit."

In *Boynton* v. *Pedrick*, supra, the court states (p. 891):

> "• • • Both the *Herberger* and the *Caldwell* cases sustained the validity of Regulation 29.41-2. It is not quite clear whether in those cases the cash receipts and disbursements method was held to 'not clearly reflect the income' as a matter of law or on the basis that a correct factual finding had been made by the Tax Court. In my opinion the cash receipts method as a matter of law does not clearly reflect income here. The regulation requires the use of an accrual method. The validity of the regulations is a question of law.
>
> "• • • But where as here, there is only one standard accounting practice, which overwhelmingly surpasses the cash receipts and disbursements method in accuracy, an accrual method of accounting is required in reporting income as a matter of law."

We agree with the reasoning of the cited cases. The regulation is reasonable and is not inconsistent with the statute upon which it is based. The regulation, under the circumstances here existing, clearly authorizes the Commissioner to insist upon the taxpayers reporting sales upon an accrual basis. The Tax Court committed no error in upholding the Commissioner's determination that the taxpayers' credit sales should be reported as income in the year of sale.

The record shows that the taxpayers have consistently used the hybrid system of accounting of which the Commissioner now complains. Previous returns have been audited and approved upon the basis of accounting used by the taxpayers in their 1947 and 1948 returns. There is no showing that the taxpayers have not acted in good faith. Nevertheless, the fact that the Commissioner accepted taxpayers' previous returns upon a cash basis without objection does not preclude him from computing the tax on the returns here involved upon an accrual basis. *Welp* v. *United States,* supra; *Caldwell* v. *Commissioner,* supra.

We now reach the question of whether taxpayers' gross income exceeded their reported gross income by more than 25 per cent.

The Commissioner insists that such excess has been established and that consequently the five year statute of limitations contained in 275(c) is applicable. Such section reads:

> "(c) *Omission from Gross Income.*—If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 5 years after the return was filed."

Since the three year statute of limitations had run when the assessments here involved were made, the decisions can be affirmed only if section 275(c) applies.

Taxpayers, citing *Wood* v. *Commissioner,* 5 Cir., 245 F.2d 888, urge that the burden is upon the Commissioner to show that the five year limitations is applicable. The *Wood* case so holds. To the same effect, see *Jack Rose* v. *Commissioner,* 24 T.C. 755, 767.

The Commissioner in this case introduced evidence which established that taxpayers had failed to report credit sales and the amount of such sales. The evidence also shows that the taxpayers' books were kept on an accrual basis, and that costs were reported for tax purposes upon the accrual basis. It also clearly appears that all items of cost and allowable deductions were claimed by the taxpayers in their original returns, and that no new or unreported costs were incurred in connection with the credit sales. The Tax Court made the following finding:

> "Respondent has established by uncontradicted evidence that credit sales properly includible in gross income were omitted from the gross receipts of the four businesses. We have set forth in our findings the amounts of credit sales unreported by the partnership in the years 1947 and 1948, and have listed the amounts of gross income reported by petitioners in their individual returns and by the businesses in the partnership returns. A comparison of the unreported credit sales figures with the individual returns discloses that each petitioner's proportionate share of the omitted amounts is far in excess of 25 per cent of the gross income stated in each corresponding individual return. * * *"

"Gross income" is not defined in the Internal Revenue Code of 1939. The parties agree that "gross income," as the term is used in section 275(c), does not mean gross receipts, but, instead, means gross receipts reduced by cost of goods sold. They also agree that the gross income stated in the taxpayers' returns includes the taxpayers' proportionate share of the partnership gross income. See *Rose* v. *Commissioner*, supra, p. 769.

The taxpayers in their brief state:

> "The nub of the inquiry in a Section 275(c) case, is stated in *H. Leslie Leas* v. *Commissioner*, 23 T.C. 1058 (1955) to be as follows:
>
> > " 'To determine whether or not section 275(c) is applicable in any year it is necessary to determine two amounts: (1) The amount of gross income "stated in the return"; and (2) the amount omitted from gross income which is "properly includible therein." '
>
> "With respect to the first of these two items, that is, the amount of gross income stated in the return, it has been consistently held that the amount which the taxpayer stated in his return is controlling and is the amount to be used in determining the application of Section 275(c) even though that amount is incorrect by reason of an overstatement or an understatement of cost of goods sold in the return. *Carew* v. *Commissioner*, 215 F.2d 58 (6 Cir. 1954); *H. Leslie Leas* v. *Commissioner, supra.*"

The Commissioner agrees that the amounts of gross income reported in the returns are established amounts, and can not be changed by either party for the purposes of section 275(c).

Taxpayers urge that, in determining the amount of gross income properly includible in the return, it is necessary to compute not only the gross receipts, but that actual cost of goods sold should also be computed and deducted from gross receipts. Taxpayers offer testimony to the effect that all costs of goods sold were not deducted in determining gross income. Taxpayers state that costs, such as expediting shipments, warehousing, conditioning, taxes on merchandise, advertising, and similar items, which properly constitute a part of the cost of goods sold, were not deducted as such costs, but, instead, were claimed by the taxpayers in their tax returns

as other deductions below line 13 of the returns. It is taxpayers' contention that, because such costs were not deducted from gross receipts in their original returns, the Commissioner can not rely upon the returns properly reflecting the cost of goods, and that the Commissioner in making the adjustments must establish the correct amounts of the cost of goods that are properly deductible from gross receipts.

Taxpayers offer testimony of an economist to support their contention that the cost of goods included the type of expenditures heretofore referred to and listed by the taxpayers as other deductions. The economist further testified that an omission occurs only when correct gross income exceeds reported gross income.

The Commissioner's position is that he has accepted the taxpayers' cost of goods sold as reported, and that he is entitled to accept such cost as reported by the taxpayer. The Commissioner also contends that parts of the various items, which the taxpayers now wish to allocate to cost of goods sold, are not reflected as cost of goods sold in the taxpayers' books; and that the propriety and amount of such deductions as an item of cost of goods sold would be dependent upon cost analysis and accounting judgment. *Wood* v. *Commissioner,* supra, relied upon by the taxpayers, is not controlling upon the issue we are considering. In the *Wood* case, the Commissioner's evidence as to the cost of land sold, for use as a basis for determining capital gain, was found by the court to be indefinite and unconvincing. The taxpayer had not reported the capital gain, and hence he did not in his return set out his cost basis.

In our present case the issue of the basis to be used for determination of capital gain is not involved. Additionally in our present case the Commissioner is accepting the cost

of goods sold figures as reported by the taxpayers. It should be pointed out that the taxpayers included in their original returns the cost of all goods sold, including the cost of goods sold on credit. The taxpayers do not contend that any expenses were incurred in connection with the credit sales that are not included in their tax returns. Taxpayers' contention that the Commissioner compared omitted gross receipts with reported gross income is without merit. All costs pertaining to the credit sales were included in the original reports. The gross income was, under the circumstances of this case, increased by the amount of the gross receipts from the credit sales.

The amounts of the credit sales were substantial. All pertinent figures are detailed in the Tax Court's opinion. The Tax Court's finding as to gross income reported, omitted sales, and percentage of omitted sales to gross income is:

1947	Gross Income	Omitted Sales	Percentage
John Iverson	$ 81,401.65	$43,994.88	54.05%
Alvilda Iverson	45,394.57	19,387.02	42.71%
Mardrid Davison	36,467.48	17,848.18	48.94%
1948			
John and Alvilda Iverson	175,184.19	52,520.80	30.50%
Mardrid Davison	51,281.18	13,039.72	25.42%

The purpose of section 275(c) is to reach substantial omissions. The taxpayers received full credit for the deductions to which they were entitled in their original returns, regardless of whether said deductions were claimed as cost of goods sold or as other deductions. The Tax Court in its opinion points out that the omitted sales are in each instance over 100 per cent of the taxpayers' net income. We are not holding that net income is the figure to be used in making computations under 275(c), but make the above observations only for the purpose of showing that the omissions are substantial.

As previously stated, all costs of goods sold are deducted from income in the original returns either above or below line 13. If the costs of goods claimed as other deductions are to be considered as costs of goods sold in determining the excess, it might be appropriate in order to make a fair comparison to make the same adjustments in the original returns. If such procedure were followed, the excess would exceed 25 per cent.

The problem presented by these cases is a difficult one. We are inclined to believe that under the peculiar facts and circumstances disclosed by the record before us the Commissioner was justified in accepting as correct the cost of goods and other deductions as reported by the taxpayers in their original returns, which for tax purposes gave taxpayers all deductions to which they were entitled. The Commissioner has in no way challenged the correctness of the cost of goods or other deductions as reported by the taxpayers. The Commissioner has proved omitted gross receipts exceeding 25 per cent of the reported gross income. All costs of goods sold, including cost of merchandise sold on credit, were claimed as credits in the original returns. Accordingly, the Tax Court was justified in determining that gross income was increased by the amount of the established credit sales, and in concluding that the omitted gross income exceeded reported gross income by 25 per cent and that the five year statute of limitations applies.

Affirmed.

A true copy.

Attest:

Clerk, U. S. Court of Appeals, Eighth Circuit

JUDGMENT

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 15,928

September Term, 1957
Friday, May 9th, 1958

ESTATE OF JOHN IVERSON, DECEASED, MARDRID DAVISON and GLADYS SORENSEN, co-executrices,
Petitioners,
v.
COMMISSIONER OF INTERNAL REVENUE.

PETITION TO REVIEW DECISION OF THE TAX COURT OF THE UNITED STATES

This cause came on to be heard on the Petition to review the decision of The Tax Court of the United States entered June 20, 1957, determining that there is a deficiency in the income tax of the petitioners for the year 1947, and was argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that the decision of the said Tax Court in this cause be, and the same is hereby affirmed.

And it is further Ordered by this Court that the said Petition to review in this cause be, and the same is hereby, dismissed.

[May 9, 1958]

JUDGMENT

UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

No. 15,929

September Term, 1957
Friday, May 9th, 1958

MARDRID REITE DAVISON,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE.

PETITION TO REVIEW DECISION OF THE TAX COURT OF THE UNITED STATES

This cause came on to be heard on the Petition to review the decision of The Tax Court of the United States entered June 20, 1957, determining that there are deficiencies in the income tax of the petitioner for the years 1947 and 1948, and was argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that the decision of the said Tax Court in this cause be, and the same is hereby affirmed.

And it is further Ordered by this Court that the said Petition to review in this cause be, and the same is hereby, dismissed.

[May 9, 1958]

JUDGMENT

UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

No. 15,930

September Term, 1957
Friday, May 9th, 1958

ESTATE OF JOHN IVERSON, DECEASED, MARDRID REITE DAVISON and GLADYS SORENSON, co-executrices, and ELLEN MYERS and CHARLOTTE SCHAEFFER, co-executrices of the ESTATE OF ALVILDA IVERSON, DECEASED,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE.

PETITION TO REVIEW DECISION OF THE TAX COURT OF THE UNITED STATES

This cause came on to be heard on the Petition to review the decision of The Tax Court of the United States entered June 20, 1957, determining that there is a deficiency in the income tax of the petitioners for the year 1948, and was argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that the decision of the said Tax Court in this cause be, and the same is hereby affirmed.

And it is further Ordered by this Court that the said Petition to review in this cause be, and the same is hereby, dismissed.

[May 9, 1958]

JUDGMENT

UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

No. 15,931

September Term, 1957
Friday, May 9th, 1958

ELLEN MYERS and CHARLOTTE SCHAEFFER, co-executrices of the ESTATE OF ALVILDA IVERSON, DECEASED,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE.

PETITION TO REVIEW DECISION OF THE TAX COURT OF THE UNITED STATES

This cause came on to be heard on the Petition to review the decision of The Tax Court of the United States entered June 20, 1957, determining that there is a deficiency in the income tax of the petitioners for the year 1947, and was argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that the decision of the said Tax Court in this cause be, and the same is hereby affirmed.

And it is further Ordered by this Court that the said Petition to review in this cause be, and the same is hereby, dismissed.

[May 9, 1958]

IN THE UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 15,928 — Civil

ESTATE OF JOHN IVERSON, ET AL.,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

No. 15,929 — Civil

MARDRID REITE DAVISON,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

No. 15,930 — Civil

ESTATE OF JOHN IVERSON, ET AL., and ELLEN MYERS and CHARLOTTE SCHAEFFER, co-executrices of the ESTATE OF ALVILDA IVERSON, DECEASED,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

No. 15,931 — Civil

ELLEN MYERS and CHARLOTTE SCHAEFFER, co-executrices of the ESTATE OF ALVILDA IVERSON, DECEASED,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

MOTION FOR RECALL OF MANDATES

The Petitioners, by their attorneys, Joseph A. Maun and William R. Busch, move the Court for recall of the mandate in each of the above-entitled cases, and in support of such motion state:

Since the decision of this Court dated May 9, 1958, was rendered, a decision which appears to be squarely in point has been handed down by the Supreme Court of the United States. That decision is *The Colony, Inc., Petitioner v. Commissioner of Internal Revenue*, United States Supreme Court, June 9, 1958, —— U.S. ——. It appears that the decision and opinion of the United States Supreme Court in that case has construed Section 275 (c) of the Internal Revenue Code of 1939 contrary to the interpretation given that section by the decision and opinion of this Court in the above-entitled cases, and therefore the mandates should be recalled.

Respectfully submitted,

JOSEPH A. MAUN
WILLIAM R. BUSCH
425 Hamm Building
St. Paul 2, Minnesota
Attorneys for Petitioners

IN THE UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 15,928 — Civil

ESTATE OF JOHN IVERSON, ET AL.,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

No. 15,929 — Civil

MARDRID REITE DAVISON,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

No. 15,930 — Civil

ESTATE OF JOHN IVERSON, ET AL., and ELLEN MYERS and CHARLOTTE SCHAEFFER, co-executrices of the ESTATE OF ALVILDA IVERSON, DECEASED,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

No. 15,931 — Civil

ELLEN MYERS and CHARLOTTE SCHAEFFER, co-executrices of the ESTATE OF ALVILDA IVERSON, DECEASED,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR REHEARING

Should this Court grant the foregoing motion for recall of the mandates in these cases and cause the mandates to be recalled, then it is respectfully submitted that the decision of this Court in each of the above-entitled cases should be reconsidered.

On June 9, 1958, the Supreme Court of the United States rendered its decision in the case of *The Colony, Inc. v. Commissioner of Internal Revenue*, U. S. Supreme Court, June 9, 1958, —— U.S. ——. A copy of that opinion is reproduced and is attached hereto as Appendix A. In that case it was necessary for the Supreme Court to construe the meaning of the critical language of Section 275 (c) of the Internal Revenue Code of 1939 involved herein, which is, "omits from gross income an amount properly includible therein." In reversing the court below, the Supreme Court flatly held that Section 275 (c) applies only to omissions of gross **receipts** and not to omissions of gross **income** as claimed by the government. The Court further held that its construction of Section 275 (c) of the 1939 Code "is in harmony with the unambiguous language of § 6501 (e) (1) (A) of the Internal Revenue Code of 1954," which specifies that the requisite minimum omission of 25% is to be determined by comparing the omitted gross **receipts** with the reported gross **receipts**.

In petitioners' original brief to this Court the following observations were made:

> "In reaching its conclusion that the petitioners were subject to assessment for the 1947 and 1948 deficiencies asserted against them in the government's statutory notices of deficiency, the Tax Court stated in its opinion below (R. 142-143):
>
> > 'A comparison of the unreported credit sales figures with the individual returns discloses that each petitioner's proportionate share of the omitted

amounts is far in excess of 25 per cent of the gross income stated in each corresponding individual return. * * * Consequently, we hold that for the years 1947 and 1948 respondent has established that petitioners omitted from gross income amounts properly includible therein which are in excess of 25 per cent of the amounts of gross income stated in the returns. It therefore follows that the notices of deficiency, which were mailed within five years after the returns were filed, were timely.'

"In so holding, the Tax Court was in error even if it be assumed, *arguendo*, that the Commissioner of Internal Revenue can unilaterally change the method of accounting which petitioners had consistently employed over the years in reporting their income. The error of the Tax Court in this regard becomes readily apparent when it is noted that the Tax Court compared 'omitted gross **receipts**' with 'reported gross **income**' in determining whether or not Section 275(c) of the 1939 Code applied. Such a comparison of unlikes, i.e., gross receipts with gross income, is, of course, wholly unwarranted. Section 275(c) of the 1939 Code provides for the comparison of the taxpayer's actual gross income with his reported gross income and specifies that the five year limitations period applies only where actual gross income exceeds reported gross income by more than 25 per cent. As indicated below, if the Tax Court had made its comparison on the proper basis, it would have found that the requisite minimum omission did not exist.

"In applying the provisions of Section 275(c) of the 1939 Code, it is necessary first to clearly fix what is meant by the term 'gross income' since the specified omission of in excess of 25 per cent relates to 'gross income.' This term is not defined in the 1939 Code, therefore it is necessary to look elsewhere for its definition. In its prior decisions, e.g., *Jack Rose v. Commissioner*, 24 T.C. 755 (1955), the Tax Court has ruled that the

'gross income' to which Section 275(c) refers is not gross receipts but is instead gross receipts reduced by the cost of goods sold. On the other hand, Section 6501 (e) (1) (i) of the Internal Revenue Code of 1954 defines 'gross income' for purposes of the extended limitations period under the 1954 Code as being equivalent to gross receipts without reduction for the cost of goods sold.

"Regardless of which of these two concepts of gross income is adopted for purposes of applying Section 275(c), it is clear that the same concept must be applied in determining both parts of the comparison so that the omission from gross income and the reported gross income are computed with a like procedure. This the Tax Court did not do, for, as the above-quoted portion of its opinion reflects, it compared omitted gross receipts with reported gross income, the latter being reported gross receipts less reported cost of goods sold.

"Had the Tax Court compared omitted gross receipts with reported gross receipts, the comparative percentage of omission as to each petitioner would have been less than 8% which is, of course, well below the requisite minimum omission of 25 per cent.[1]

[1] "Thus for 1947 John Iverson's reported gross receipts from business and nonbusiness sources was $573,560.56 (R. 135, 137) and his share of the uncollected credit sales for that year was $43,994.88 (R. 137). This made his accrual basis gross receipts $617,555.44 which is but 7.67% more than reported on the cash basis. Alvilda Iverson's reported gross receipts on the cash basis in 1947 were $309,797.62 (R. 135, 138) and her share of the uncollected credit sales for that year was $19,387.02 (R. 137). Her accrual basis receipts were therefore $329,184.64 which is 6.26% more than reported on cash. For 1948, John and Alvilda Iverson jointly reported gross receipts of $1,351,898.71 (R. 135, 138) and their share of the uncollected credit sales for the year was $52,520.80 (R. 137). Their accrual basis gross receipts therefore exceeded reported gross receipts by only 3.88%. Mardrid Davison reported gross receipts of $234,066.13 and $367,189.73, respectively, for 1947 and 1948 (R. 135, 138). Her share for 1948 (R. 137). Her accrual basis gross receipts therefore exceeded her reported gross receipts by only 7.63% in 1947 and of uncollected credit sales was $17,848.18 for 1947 and $13,039.72 3.55% in 1948."

The undisputed fact in the instant cases is that there was not an omission of more than 25% of the reported gross receipts. Under the foregoing decision of the United States Supreme Court then, where the omission from gross receipts is less than 25% of the reported gross receipts, the statute of limitations is not held open for the 5-year period under Section 275 (c). This Court, however, held in the instant cases that in view of the fact that the omission of gross receipts was more than 25% of the reported gross profit, the statute of limitations was held open under Section 275 (c).

The Supreme Court of the United States, in its opinion in *The Colony, Inc.*, supra, made the following observations:

> "We granted certiorari because this decision conflicted with rulings in other Courts of Appeals on the same issue, and because the question as to the proper scope of § 275(c), although resolved for the future by § 6501 (e)(1)(A) of the Internal Revenue Code of 1954, p. —, infra, remains one of substantial importance in the administration of the income tax laws for earlier taxable years.
>
> • • • • •
>
> "Finally, our construction of § 275(c) accords with the interpretations in the more recent decisions of four different Courts of Appeals. See note 2, supra. The force of the reasoning in these opinions was recognized by the Court of Appeals in the present case, which indicated that it might have agreed with those courts had the matter been res nova in its circuit. 244 F. 2d at 76. And without doing more than noting the speculative debate between the parties as to whether Congress manifested an intention to clarify or to change the 1939 Code, *we observe that the conclusion we reach is in harmony with the unambiguous language of § 6501(e)(1)(A)* of the *Internal Revenue Code of 1954*." (Emphasis supplied.)

Section 6501 (e) (1) (A) of the Internal Revenue Code of 1954 referred to by the Supreme Court of the United States provides as follows:

"§ 6501. Limitations on assessment and collection.

"(e) Omission from gross income.—Except as otherwise provided in subsection (c)—

"(1) Income taxes.—In the case of any tax imposed by subtitle A—

"(A) General rule.—If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per cent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—

"(i) In the case of a trade or business, the term, 'gross income' means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and

"(ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary or his delegate of the nature and amount of such item."

The first paragraph of Section 6501 (e) (1) (A) is identically the same in wording as Section 275 (c) of the Internal Revenue Code of 1939 except that the time limit is 6 years instead of 5. However, the second paragraph of Section 6501 (e) (1) (A) specifically defines the term "gross income" to be "gross receipts," that is, the total amounts received or accrued from the sale of goods or services *prior* to diminution by the cost of such sales or services.

It is this definition of "gross income" that the Supreme Court has specifically adopted in construing Section 275 (c) of the 1939 Code, with the result that "gross income" is to be treated as synonymous with "gross receipts" for purposes of applying Section 275 (c). This, of course, is exactly contrary to the hypothesis upon which this Court bottomed its decision in these cases and contrary, of course, to the position of the Commissioner of Internal Revenue. In view of the undisputed fact that none of the petitioners herein omitted an amount of gross receipts, even on the accrual basis of accounting, that is in excess of 25% of his reported gross receipts or, in other words, "gross income" as computed prior to diminution by the cost of sales, it is submitted that this Court should reconsider its decision.

Respectfully submitted,

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Attorneys for Petitioners

CERTIFICATE OF COUNSEL

We hereby certify in compliance with Rule 15 (b) of this Court that this petition is filed in good faith and is believed to be meritorious.

JOSEPH A. MAUN
WILLIAM R. BUSCH
Attorneys for Petitioners

APPENDIX A

No. 306—October Term, 1957

THE COLONY, INC.,
Petitioner,
v.
COMMISSIONER OF INTERNAL REVENUE.

On Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit.
[June 9, 1958]

Mr. JUSTICE HARLAN delivered the opinion of the Court.

The sole question in this case is whether assessments by the Commissioner of two asserted tax deficiencies were barred by the three-year statute of limitations provided in the Internal Revenue Code of 1939.

Under the 1939 Code the general statute of limitations governing the assessment of federal income tax deficiencies is fixed at three years from the date on which the taxpayer filed his return, § 275 (a), 53 Stat. 86, except in cases involving intentionally false or fraudulent returns, where a tax may be assessed at any time. § 275 (c), 53 Stat. 87. A special five-year period of limitations is provided when a taxpayer, even though acting in good faith, "omits from gross income an amount properly includible therein which is in excess of

25 per centum of the amount of gross income stated in the return * * *." §275 (c), 53 Stat. 86. In either case the period of limitation may be extended by a written waiver executed by the taxpayer within the statutory or any extended period of limitation. § 276 (b), 53 Stat. 87.[1]

The Commissioner assessed deficiencies in the taxpayer's income taxes for each of the fiscal years ending October 31, 1946, and 1947, within the extended period provided in waivers which were executed by the taxpayer more than three but less than five years after the returns were filed. There was

[1] The pertinent provisions of the 1939 Code are:

"SEC. 275. PERIOD OF LIMITATION UPON ASSESSMENT AND COLLECTION.

"Except as provided in section 276—

"(a) GENERAL RULE.—The amount of income taxes imposed by this chapter shall be assessed within three years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period.

* * *

"(c) OMISSION FROM GROSS INCOME.—If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 per centum of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 5 years after the return was filed.

"SEC. 276. SAME—EXCEPTIONS.

"(a) FALSE RETURN AND NO RETURN.—In the case of a false or fraudulent return with intent to evade tax or of a failure to file a return the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time.

"(b) WAIVER.—Where before the expiration of the time prescribed in section 275 for the assessment of the tax, both the Commissioner and the taxpayer have consented in writing to its assessment after such time, the tax may be assessed at any time prior to the expiration of the period agreed upon. The period so agreed upon may be extended by subsequent agreements made before the expiration of the period previously agreed upon."

no claim that the taxpayer had inaccurately reported its gross receipts. Instead, the deficiencies were based upon the Commissioner's determination that the taxpayer had understated the gross profits on the sales of certain lots of land for residential purposes as the result of having overstated the "basis" of such lots by erroneously including in their cost certain unallowable items of development expense. There was no claim that the returns were fraudulent.

The Tax Court sustained the Commissioner. It held that substantial portions of the development costs were properly disallowed, and that these errors by the taxpayer had resulted in the understatement of the taxpayer's total gross income by 77.2% and 30.7%, respectively, of the amounts reported for the taxable years 1946 and 1947. In addition, the Tax Court held that in these circumstances the five-year period of limitation provided for in § 275 (c) was applicable. It took the view that the statutory language, "omits from gross income any amount includible therein," embraced not merely the omission from a return of an item of income received by or accruing to a taxpayer, but also an understatement of gross income resulting from a taxpayer's miscalculation of profits through the erroneous inclusion of an excessive item of cost. 26 T.C. 30. On the taxpayer's appeal to the Court of Appeals the only question raised was whether the three-year or the five-year statute of limitations governed the assessment of these deficiencies. Adhering to its earlier decision in *Reis* v. *Commissioner*, 142 F. 2d 900, the Court of Appeals affirmed. 244 F. 2d 75. We granted certiorari because this decision conflicted with rulings in other Courts

of Appeals on the same issue,[2] and because the question as to the proper scope of § 275 (c), although resolved for the future by § 6501 (e) (1) (A) of the Internal Revenue Code of 1954, p. —, *infra*, remains one of substantial importance in the administration of the income tax laws for earlier taxable years. 355 U.S. 811.

In determining the correct interpretation of § 275 (c) we start with the critical statutory language, "omits from gross income an amount properly includible therein." The Commissioner states that the draftsman's use of the word "amount" (instead of, for example, "item") suggests a concentration on the quantitative aspect of the error—that is, whether or not gross income was understated by as much as 25%. This view is somewhat reinforced if, in reading the above-quoted phrase, one touches lightly on the word "omits" and bears down hard on the words "gross income," for where a cost item is overstated, as in the case before us, gross income

[2] In conflict with this case are decisions in four different Courts of Appeals. *Uptegrove Lumber Co.* v. *Commissioner*, 204 F. 2d 570 (C. A. 3d Cir.); *Deakman-Wells Co.* v. *Commissioner*, 213 F. 2d 894 (C. A. 3d Cir.); *Slaff* v. *Commissioner*, 220 F. 2d 65 (C. A. 9th Cir.); *Davis* v. *Hightower*, 230 F. 2d 549 (C. A. 5th Cir.); *Goodenow* v. *Commissioner*, 238 F. 2d 20 (C. A. 8th Cir.). The Court of Claims has also held to the contrary of the present case. *Lazarus* v. *Commissioner*, 142 F. Supp. 897.

Three Courts of Appeals decisions antedating *Uptegrove Lumber Co.* v. *Commissioner*, *supra*, provided support for the Government's construction of § 2752(c). *Foster's Estate* v. *Commissioner*, 131 F. 2d 405 (C. A. 5th Cir.); *Ketcham* v. *Commissioner*, 142 F. 2d 996 (C. A. 2d Cir.); *O'Bryan* v. *Commissioner*, 148 F. 2d 456 (C. A. 9th Cir.). But neither *Foster's Estate* nor *O'Bryan* can be regarded as the controlling authority within their respective circuits in view of the more recent decisions in *Davis* v. *Hightower*, *supra*, and *Slaff* v. *Commissioner*, *supra*. *Ketcham* is distinguishable on its facts.

The Sixth Circuit has consistently maintained its current position. The Tax Court has also regularly upheld the Commissioner. *E.g.*, *American Liberty Oil Co.* v. *Commissioner*, 1 T. C. 386; *Estate of Gibbs* v. *Commissioner*, 21 T. C. 443.

is affected to the same degree as when a gross receipt item of the same amount is completely omitted from a tax return.

On the other hand, the taxpayer contends that the Commissioner's reading fails to take full account of the word "omits," which Congress selected when it could have chosen another verb such as "reduces" or "understates," either of which would have pointed significantly in the Commissioner's direction. The taxpayer also points out that normally "statutory words are presumed to be used in their ordinary and usual sense, and with the meaning commonly attributable to them." *DeGanay* v. *Lederer,* 250 U.S. 376, 381. "Omit" is defined in Webster's New International Dictionary (2d ed. 1938) as "to leave out or unmentioned; not to insert, include or name," and the Court of Appeals for the Sixth Circuit has elsewhere similarly defined the word. *Ewald* v. *Commissioner,* 141 F. 2d 750, 753. Relying on this definition, the taxpayer says that the statute is limited to situations in which specific receipts or accruals of income items are *left out* of the computation of gross income. For reasons stated below we agree with the taxpayer's position.

Although we are inclined to think that the statute on its face lends itself more plausibly to the taxpayer's intepretation, it cannot be said that the language is unambiguous. In these circumstances we turn to the legislative history of § 275 (c). We find in that history persuasive evidence that Congress was addressing itself to the specific situation where a taxpayer actually omitted some income receipt or accrual in his computation of gross income, and not more generally to errors in that computation arising from other causes.

Section 275 (c) first appeared in the Revenue Act of 1934. 48 Stat. 680. As introduced in the House the bill simply added the gross-income provision to § 276 of the Revenue Act

of 1932, 47 Stat. 168, relating to fraudulent returns and cases where no return had been filed, and carried with it no period of limitations. The intended coverage of the proposed provision was stated in a Report of a House Ways and Means Subcommittee as follows:

> "Section 276 provides for the assessment of the tax without regard to the statute of limitations in case of a failure to file a return or in case of a false or fraudulent return with intent to evade tax.
>
> "Your subcommittee is of the opinion that the limitation period on assessment should also not apply to certain cases where the taxpayer has understated his gross income on his return by a large amount, even though fraud with intent to evade tax cannot be established. It is, therefore, recommended that the statute of limitations shall not apply where the taxpayer has failed to disclose in his return an amount of gross income in excess of 25 percent of the amount of the gross income stated in the return. The Government should not be penalized where a taxpayer is so negligent as to leave out items of such magnitude from his return." House Hearings before Committee on Ways and Means, 73d Cong., 2d Sess., p. 139.

This purpose of the proposal was related to the full Committee in the following colloquy between Congressman Cooper of Tennessee, speaking for the Subcommittee, and Mr. Roswell Magill, representing the Treasury:

> "Mr. Cooper: What we really had in mind was just this kind of situation: Assume that a taxpayer left out, say a million dollars; he just forgot it. We felt that whenever we found that he did that we ought to get the money on it, the tax on it.
>
> "Mr. Magill: I will not argue against you on that score.

"Mr. Cooper: In other words, if a man is so negligent and so forgetful, or whatever the reason is, that he overlooks an item amounting to as much as 25 percent of his gross income, that we simply ought to have the opportunity of getting the tax on that amount of money." House Hearings, *supra*, p. 149.

The full Committee revealed the same attitude in its report:

"It is not believed that taxpayers who are so negligent as to leave out of their returns items of such magnitude should be accorded the privilege of pleading the bar of the statute." H. R. Rep. No. 704, 73d Cong., 2d Sess., p. 35.

The Senate Finance Committee approved of the intended coverage and language of the bill, except that it believed the statute of limitations should not be kept open indefinitely in the case of an honest but negligent taxpayer. Its report stated:

"* * * Your committee is in general accord with the policy expressed in this section of the House bill. However, it is believed that in the case of a taxpayer who makes an honest mistake, it would be unfair to keep the statute open indefinitely. For instance, a case might arise where a taxpayer failed to report a dividend because he was erroneously advised by the officers of the corporation that it was paid out of capital or he might report as income for one year an item of income which properly belonged in another year. Accordingly, your committee has provided for a 5-year statute in such cases." S. Rep. No. 558, 73d Cong., 2d Sess., pp. 43-44.

Except for embodying the five-year period of limitation, § 275 (c), as passed, reflects no change in the original basic objective underlying its enactment.

As rebutting these persuasive indications that Congress merely had in mind failures to report particular income receipts and accruals, and did not intend the five-year limitation to apply whenever gross income was understated, the Commissioner stresses the occasional use of the phrase "understates gross income" in the legislative materials. The force of this contention is much diluted, however, when it is observed that wherever this general language is found its intended meaning is immediately illuminated by the use of such phrases as "failed to disclose" or "to leave out" items of income. See *Uptegrove Lumber Co.* v. *Commissioner*, 204 F. 2d 570, 572.

The Commissioner also suggests that in enacting § 275 (c) Congress was primarily concerned with providing for a longer period of limitations where returns contained relatively large errors adversely affecting the Treasury, and that effect can be given this purpose only by adopting the Government's broad construction of the statute. But this theory does not persuade us. For if the mere size of the error had been the principal concern of Congress, one might have expected to find the statute cast in terms of errors in the total tax due or in total taxable net income. We have been unable to find any solid support for the Government's theory in the legislative history. Instead, as the excerpts set out above illustrate, this history shows to our satisfaction that the Congress intended an exception to the usual three-year statute of limitations only in the restricted type of situation already described.

We think that in enacting § 275 (c) Congress manifested no broader purpose than to give the Commissioner an additional two years to investigate tax returns in cases where,

because of a taxpayer's omission to report some taxable item, the Commissioner is at a special disadvantage in detecting errors. In such instances the return on its face provides no clue to the existence of the omitted item. On the other hand, when, as here, the understatement of a tax arises from an error in reporting an item disclosed on the face of the return the Commissioner is at no such disadvantage. And this would seem to be so whether the error be one affecting "gross income" or one, such as overstated deductions, affecting other parts of the return. To accept the Commissioner's interpretation and to impose a five-year limitation when such errors affect "gross income," but a three-year limitation when they do not, not only would be to read § 275 (c) more broadly than is justified by the evident reason for its enactment, but also to create a patent incongruity in the tax law. See *Uptegrove Lumber Co.* v. *Commissioner*, *supra*, at 573.

Finally, our construction of § 275 (c) accords with the interpretations in the more recent decisions of four different Courts of Appeals. See note 2, *supra*. The force of the reasoning in these opinions was recognized by the Court of Appeals in the present case, which indicated that it might have agreed with those courts had the matter been *res nova* in its circuit. 244 F. 2d, at 76. And without doing more than noting the speculative debate between the parties as to whether Congress manifested an intention to clarify or to change the 1939 Code, we observe that the conclusion we reach is in harmony with the unambiguous language of

§ 6501 (e) (1) (A) of the Internal Revenue Code of 1954.[3]

We hold that both tax assessments before us were barred by the statute of limitations.

Reversed.

THE CHIEF JUSTICE and MR. JUSTICE BLACK would follow the interpretation consistently given § 275 (c) by the Tax Court for many years and affirm the judgment of the Court of Appeals in this case. See cases cited in Note 2 of the Court's opinion.

A. ROBERT DOLL (S. L. GREENEBAUM, B. H. BARNETT, CHARLES F. WOOD, GREENEBAUM, BARNETT & WOOD, and RICHARD C. OLDHAM, with him on the brief) for petitioner; JOSEPH F. GOETTEN (J. LEE RANKIN, Solicitor General, CHARLES K. RICE, Assistant Attorney General, and GRANT W. WIPRUD, with him on the brief) for respondent.

[3] "§ 6501. Limitations on assessment and collection.

* * *

"(e) Omission from gross income.—Except as otherwise provided in subsection (c)—

"(1) Income taxes.—In the case of any tax imposed by subtitle A—

"(A) General rule.—If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—

"(i) In the case of a trade or business, the term 'gross income' means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and

"(ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary or his delegate of the nature and amount of such item."

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

15,928–15,931

ESTATE OF JOHN IVERSON, ET AL.,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent,

AND RELATED CASES.

ON MOTION FOR RECALL OF MANDATES AND LEAVE TO FILE PETITION FOR REHEARING

[July 25, 1958]

SUPPLEMENTAL OPINION

Before GARDNER, Chief Judge, and VOGEL and VAN OOSTERHOUT, Circuit Judges.

PER CURIAM.

Our opinion in these cases affirming the decision of the Tax Court against the petitioning taxpayers was filed on May 9, 1958. The opinion is reported at 255 F.2d 1. Taxpayers on June 23, 1958, lodged with the Clerk of this Court motion for recall of mandates and petition for rehearing.

We shall treat the motion for recall of mandates as properly filed and shall consider said motion. Since the term at which the judgments of this court were entered is still open, we shall assume that this court has jurisdiction to recall the

mandates. The mandates were properly issued on June 16, 1958, pursuant to our Rule 16. The time for filing petition for rehearing had then expired. We believe that our power to recall mandates should be exercised sparingly. The showing made in the present motion is not adequate to warrant the recall of the mandates.

We also believe that leave to file petition for rehearing should be denied. With the mandates on the judgments here involved outstanding, it is doubtful whether this court would have jurisdiction to consider a petition for rehearing. In any event, we do not believe that a showing such as to entitle taxpayers to file a petition for rehearing out of time has been made. Our Rule 15(a) requires that petitions for rehearing be filed "not later than 20 days after the filing of an opinion." Said rule should be strictly complied with. See 3 Am. Jur. Appeal & Error, § 802. Here, no attempt was made to file the petition for rehearing until June 23, 1958, some 45 days after the filing of the opinion. This was 25 days after the expiration of the time for filing petition for rehearing under the rule. The only reason assigned for the late filing of the petition is the taxpayers' contention that the Supreme Court, in *The Colony, Inc.* v. *Commissioner of Internal Revenue*, —— U.S. ——, decided June 9, 1958, decided an issue pertinent to this appeal favorably to them. It is neither necessary nor proper for our present purpose to determine the validity of such contention. The appellate rules are designed to bring about an orderly and prompt termination of litigation. If the rule regulating the time for filing petitions for rehearing is to be relaxed to meet a situation such as here presented, what time limit is to be imposed? If a petition can be filed 25 days after the expiration of the time granted for filing, can such a petition be filed 3 months, 6 months, or a year

after the judgment has become final? We believe that the time granted for filing petitions for rehearing by our rules is reasonable and that it should be adhered to, and that any substantial departure from the time fixed by the rule would lead to hopeless confusion.

The motion for recall of mandates is overruled. Leave to file petition for rehearing is denied.

A true copy.

Attest:

Clerk, U. S. Court of Appeals, Eighth Circuit